UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, and Joseph T. Kelliher.

Southern California Edison Company on behalf of Mountainview Power Company, LLC — Docket No. ER04-316-001

ORDER ON REHEARING

(Issued October 28, 2004)

1. On February 25, 2004, the Commission conditionally accepted a Power Purchase Agreement (PPA) between Southern California Edison Company (Edison) and Mountainview Power Company, LLC (Mountainview).[1] Mountainview owned a yet-to-be completed generating plant, and Edison sought to exercise an option to purchase the project by purchasing Mountainview. The order accepted the PPA and imposed conditions to minimize any impacts on the competitive wholesale power market in California. The order also established a new policy for affiliate transactions filed in the future, requiring that all long-term (one year or longer) power purchase agreements between affiliates, whether cost-based or market-based, be subject to the conditions set forth in *Boston Edison Co. Re: Edgar Electric Energy Co.* (*Edgar*), 55 FERC ¶ 61,382 (1991). This order denies rehearing of the February 25 Order on all issues but one, as discussed below. This action benefits customers by accommodating the construction of new generation in California while ensuring that Mountainview's rates are just and reasonable.

I. **Background**

2. On December 19, 2003, Edison filed the proposed PPA on behalf of Mountainview, its to-be-acquired subsidiary. Mountainview owned a yet-to-be completed 1,054 MW state-of-the-art generating plant. Edison sought to exercise an option to purchase the project by purchasing Mountainview from its previous owner, Sequoia Generating LLC (Sequoia). Edison claimed that its purchase of Mountainview

[1] Southern California Edison Company, On Behalf of Mountainview Power Company, LLC, 106 FERC ¶ 61,183 (2004) (February 25 Order).

would restore stability to the marketplace, enhance reliability and provide substantial benefits to Edison's ratepayers, but Edison requested Commission approval of the PPA before it exercised its option. The PPA is a cost-based rate schedule which includes ratemaking features that give Mountainview incentives to control discretionary costs that it will incur and pass on to Edison.

3. Edison stated that it elected to use the subsidiary-PPA structure because it was just beginning to return to financial health, and because significant unresolved policy issues in California "demand the increased assurance of cost recovery that a FERC-filed, cost-based PPA provides."[2] The utility asserted that the unique proposal was entered into because of the urgent need for new generating capacity in California. Edison noted that the California Public Utilities Commission (CPUC) found that the transaction is in the public interest and made other findings required by the Public Utility Holding Company Act of 1935 (PUHCA).

4. In the February 25 Order, the Commission found the proposed cost-based rate to be just and reasonable but conditioned its approval on Edison modifying the PPA in several areas, filing under section 205 when it seeks to recover decommissioning costs, making a section 205 filing prior to commercial operation to establish the rate of return to support the then-applicable cost of capital, and on Mountainview complying with Commission regulations applicable to traditional public utilities, including maintaining its books in accordance with the Uniform System of Accounts, and filing a FERC Form No. 1 on an annual basis. In addition, the Commission conditioned its approval on the applicants agreeing that Mountainview be created and formed solely for the purpose of owning the Mountainview project and selling the output to Edison at cost-based rates under the PPA, on Mountainview not being eligible to sell at market-based rates, and not being entitled to any waivers typically granted under the Commission's market-based rate program.

II. <u>Requests For Rehearing and Motion To Lodge</u>

5. The requests for rehearing of the Independent Energy Producers Association (IEP), Calpine Corporation (Calpine), and the Electric Power Supply Association and Western Power Trading Forum (jointly, Competitive Suppliers) raise affiliate transaction issues. These parties also contend that the Commission erred in accepting, without hearing, the PPA's terms. In addition, the Cogeneration Association of California (CAC) objects that the Commission should have conditioned its approval of the PPA on Edison's compliance with the Public Utility Regulatory Policies Act of 1978 (PURPA). Finally, Public Service Electric and Gas Company, PSEG Energy Resources and Trade LLC and PSEG Power LLC (collectively, PSEG Companies) filed a motion to intervene out-of-

[2] Edison transmittal letter at 3.

time and request for clarification and alternative request for rehearing. PSEG Companies do not challenge the February 25 Order's treatment of the PPA, but only request clarification or rehearing concerning the scope of the new affiliate transaction policy.

6. On April 12, 2004, Edison filed a motion for leave to respond and a response to several rehearing requests. Subsequently, IEP filed for leave to respond to Edison's pleading, asking that the Commission reject Edison's response or, alternatively, accept IEP's reply.

7. On June 4, 2004, Calpine filed a motion to lodge an excerpt from the *US and the Americas Investment Report*, which discusses the impact of Edison's acquisition of the Mountainview project from an investment perspective. Calpine also requests expedited action on the pending rehearing requests. There were no responses to Calpine's motion.

III. Discussion

A. Procedural Matters

8. When late intervention is sought after the issuance of a dispositive order, the prejudice to other parties and burden upon the Commission of granting the late intervention may be substantial. Thus, movants bear a higher burden to demonstrate good cause for granting such late intervention.[3] PSEG Companies have not met this higher burden of justifying their late intervention. In light of our decision to deny PSEG Companies' late motion to intervene, we will dismiss their request for rehearing. Because PSEG Companies are not parties to this proceeding, they lack standing to seek rehearing of the February 25 Order under the Federal Power Act (FPA) and the Commission's regulations.[4]

9. Rule 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.713 (2004), prohibits an answer to a rehearing request. Accordingly, we will reject Edison's answer and likewise dismiss IEP's answer.

B. Cost Based Features

1. Acquisition Adjustment

10. In the February 25 Order, the Commission found the PPA's formula rate, as conditioned, to be reasonable, but predicated the finding on "Mountainview including only the actual purchase cost with no premium or acquisition adjustment thereto for

---

[3] *See*, *e.g.*, Midwest Independent Transmission System Operator, Inc., 102 FERC ¶ 61,250 at P 7 (2003).

[4] 16 U.S.C. § 825l(a) (2000); 18 C.F.R. § 385.713(b) (2004).

inclusion in capital costs."[5] Calpine argues on rehearing that the installed cost of the Mountainview facility fails to reflect a purported $415 million "write-down" by the former owner of the facility, AES Corporation (AES). Calpine states that AES reported the write-down to the Securities and Exchange Commission in a Form 10-K filing earlier this year. Calpine asserts that AES' selling the facility at less than cost means that Edison's shareholders are receiving the benefit of the distressed asset and that ratepayers are saddled with the consequence of a high-cost affiliate transaction.

11. We disagree with Calpine that any write-down of the Mountainview facility will inure to the benefit of Edison's shareholders. We made clear in the February 25 Order that Edison may not adjust the cost of the facility above its purchase price to reflect its actual value, if indeed its monetary value exceeds the purchase price. Although that information was not in the record at the time of the February 25 Order, Edison will report the purchase price, among other things, in a section 205 filing prior to commercial operation. Edison will not be allowed to pass along any type of premium or acquisition adjustment to its ratepayers.

12. We also note that AES did not sell the facility directly to Edison, but rather to Sequoia Generating LLC, which then sold it to Edison.[6] Thus, AES' financial dealings have no direct bearing on Edison's rates and offer no proof of excessive rates.

13. For these reasons, we will deny Calpine's motion to lodge an excerpt from the *US and the Americas Investment Report* discussing the impact of Edison's acquisition from an investment perspective. The opinion of the investment community, while noteworthy, is not relevant to the assessment of whether the cost-based rate can be found just and reasonable. Even if acquiring this project has added value for Edison's shareholders, this does not lead to a conclusion that the rate is excessive. Edison is precluded from including anything more than the total actual cost of the project in its rates, including the purchase price, costs incurred to complete the project and AFUDC. Therefore, the extraneous information in the investment report is not needed in the record of this proceeding.

2. **Piecemeal Review**

14. IEP argues on rehearing that the Commission erred in allowing the piecemeal review of the PPA's cost components, rather than in a single setting. IEP asserts that allowing Mountainview to submit its required cost information through multiple filings (*i.e.*, compliance, informational and section 205) imposes unnecessary burdens on the parties, making it more likely that the full impact of this transaction will escape without

---

[5] February 25 Order at P 27.

[6] *See id*. at P 2 & n.2.

appropriate scrutiny. IEP further contends that our requirement that parties challenge the implementation of the incentive provisions in a complaint filed under FPA section 206[7] improperly shifts the burden to third parties to ensure that the PPA is just and reasonable.

15. We will deny IEP's request for rehearing on this issue. First, we note that Edison in its initial filing proposed two commitments: (1) that Mountainview would file prior to commercial operation to implement the then applicable CPUC-approved cost of capital for Edison's utility's assets; and (2) that Mountainview would file, on January 1 of each year, to adjust the cost of capital used in the formula rate to reflect the then-effective cost of capital allowed by the CPUC. Our February 25 Order accepted Edison's commitment to file under section 205 of the FPA, prior to commercial operation, support for its proposed capital structure and return on common equity and, in addition, required Mountainview to make, on an annual basis, a May 1 informational filing detailing the prior calendar year's costs concurrent with the filing of a FERC Form No. 1. The Commission stated that, subsequent to the pre-commercial operation filing, it would determine the justness and reasonableness of the cost of capital components, and specifically stated that the Commission would address IEP's concerns as to the basis for the return on equity, including whether it is appropriate for the return on equity to be based on the regulated utility's assets. Thus, the Commission did not specifically require that Mountainview make a January 1 annual filing related to the appropriate cost of capital because Edison's filing commitment, after commencement of commercial operation, was specifically tied to reflect the then-effective cost of capital allowed by the CPUC, and the appropriateness of the use of the CPUC cost of capital will be determined in the section 205 filing that Mountainview will make prior to commercial operation.

16. It is reasonable, and indeed necessary, to require future filings for the submission of data that will only be available at a later point in time, such as the actual calendar year costs to be submitted in informational filings. This information was not available at the time of Edison's initial application, and requiring future filings to allow for an on-going review of actual costs incurred is appropriate.

17. We will clarify that parties will be able to comment on the informational filings to be filed on May 1 of each year. To the extent the data indicate any problems, parties may then file a complaint, or the Commission may institute an investigation on its own initiative, under FPA section 206 at that time. Similarly, the Commission's accepting of the incentive provisions in the PPA was predicated on parties having the right to contest their reasonableness on a going forward basis in a complaint. We found the incentive mechanisms proposed in the initial application to be just and reasonable; thus Edison met its burden under section 205. The burden of proving any future challenge is appropriately on other parties or the Commission, pursuant to section 206.

[7] *See id*. at P 41.

18. We find that the separate filings ordered by the Commission are reasonable and will not result in a piecemeal review of the PPA's components or an unnecessary burden on the parties. Specifically, Mountainview submitted a compliance filing, as required, in response to the February 25 Order. This compliance filing ensures that the PPA is revised to reflect the Commission's findings in its February 25 Order. Additionally, while the Commission also required Mountainview to make a section 205 filing to justify the recovery of decommissioning costs, that filing will ensure that Mountainview's recovery of decommissioning costs under the PPA is just and reasonable. Therefore, while we have required Mountainview to make a number of separate filings, this approach is consistent with our approach in other cost-based rate proceedings and will ensure that Mountainview's PPA results in just and reasonable rates.

3. Cost-of Service Issues

19. IEP states that the Commission failed to address three cost-of-service issues raised by IEP in its protest; specifically: (1) whether the recovery of interconnection costs through the Pre-Authorization Charge is consistent with Order No. 2003;[8] (2) the appropriateness of including in the Pre-Authorization Charge prior claims by Edison employees who worked at the now non-operational power plant at the Mountainview site; and (3) the necessity for further review and discovery to determine the potential impact of decommissioning costs on the capital Recovery Charge.

20. With respect to the interconnection costs, it is our understanding that the PPA will recover those costs that Mountainview incurs in interconnecting its facilities with Edison. Any costs included in the PPA must be consistent with Commission policy as articulated in Order No. 2003. To the extent that IEP believes that any interconnection costs included in the PPA are inappropriate, it may raise that issue in response to Mountainview's annual May 1 informational filing.

21. With respect to IEP's concerns regarding decommissioning costs, we find that IEP's concerns are premature. The Mountainview plant is anticipated to be in service for thirty years, and the collection of such costs of this nature are often difficult to predict with any accuracy in the early years of operation.

22. Finally, regarding IEP's argument that cost claims by former Edison employees, we will grant rehearing. In its original submittal, Edison included in the Pre-Authorization Charge a category of costs called "all Prior Claims with respect to the Facility." These Prior Claims were against Mountainview with respect to the Facility prior to its ownership by Mountainview which may include claims by Edison employees

---

[8] *Standardization of Generation Interconnection Agreements and Procedures*, Order No. 2003, FERC Stats. & Regs. P 31,146 (2003), *order on reh'g*, Order No. 2003-A, 106 FERC ¶ 61,220 (2004).

who worked at the now non-operational power plant that is located on the site. IEP argues that it is not appropriate to include such costs in the PPA because it does not appear that the old plant provides any benefits to future ratepayers. We agree. Additionally, Edison has not provided support for the inclusion of these costs. Furthermore, the Commission is generally opposed to including prior period costs in future rates, inasmuch as these costs should have been recovered on a timely basis in other rate forums.[9] Therefore, we will grant rehearing on this issue, and we will require Edison, on behalf of Mountainview, to submit a compliance filing within 30 days revising the PPA in this regard.

4. Additional Conditions

23. IEP states that the Commission erred in not imposing additional conditions on the PPA such as: (1) Edison providing details on the interconnection costs; (2) Edison filing a study which examines the impact of its dispatch decisions with respect to the Mountainview plant on transmission constraints faced by competing sellers; (3) all Operation and Maintenance costs being examined and tracked collectively through one charge or mechanism; (4) Edison including in a compliance filing the results of the heat rate and availability incentive proposals.

24. We will deny IEP's request for rehearing on these issue. Most of these arguments were raised by IEP in its protest to the original Mountainview filing. The Commission imposed numerous conditions and filing requirements on the PPA; thus, most of these rehearing arguments have already been addressed. With respect to Edison studying the impact of its dispatch decisions, we find that this request has nothing to do with the justness and reasonableness of the rates in the PPA. The issue of whether Edison could exercise vertical market power through strategic dispatch of Mountainview is discussed below.

5. Incentive Provisions

25. There are two performance measurements, or targets, in the PPA, an availability measurement (actual availability measured against the contract's availability target) and a heat rate incentive. In the February 25 Order, the Commission found the proposed incentives reasonable. The Commission determined that the heat rate incentives, which reflect either payments for additional gas costs incurred or savings from maintaining the target heat rate, are representative of expectations for this type of unit and are consistent with other incentive arrangements, and found that the target availability relied upon is a valid comparable measure. The Commission noted that if parties believe, based on future annual informational filings, that these incentives are not just and reasonable, they may file a complaint at that time.

[9] *See, e.g., Enbridge Pipelines (KPC)*, 109 FERC ¶ 61,042 at P 40, 42 (2004).

26. IEP argues on rehearing that requiring parties to challenge the incentive provisions of the PPA in a section 206 complaint improperly shifts the burden to intervenors to ensure that the rates, terms, and conditions of the PPA are just and reasonable. Additionally, IEP argues that the February 25 Order ignores virtually all issues raised by IEP concerning the incentive proposals, including: (1) the use of, and cost-tracking capabilities of escalation indexes; (2) the use of a single source for the indices; (3) the use of non-cost-based automatic adjustments for the availability incentives; and (4) the lack of support for the proposed payment and penalty levels for the availability incentive. Citing the Commission's *Incentive Ratemaking Policy Statement*,[10] IEP states that the PPA should not have been accepted with incentive mechanisms since the Commission has made clear that, where a competitive market exists, incentive rates should not be used.

27. The Commission rejects IEP's argument that the Commission has improperly shifted the burden to third parties regarding the incentive provisions. Edison had the burden of proof in this proceeding to show that its proposed performance targets were just and reasonable. The Commission found the proposed PPA, including the incentive provisions, to be just and reasonable, subject to Edison submitting a compliance filing and other annual filings. The burden was on Edison to establish the justness and reasonableness of the PPA, and that burden was met. As stated in the February 25 Order, if parties believe that these provisions are no longer just and reasonable based on the required annual informational filings, they may file a complaint at that time detailing their concerns, and the Commission may adjust those charges if found to be unjust or unreasonable. This is the Commission's established practice for formula rates.[11]

28. Regarding the argument that the PPA should not have been accepted with incentive mechanisms because a competitive market exists, we deny IEP's rehearing request. Cost-based rates, like those in the PPA, are an option that current market participants in California and elsewhere have. The Commission has always considered specific incentive rate proposals as tools to optimize efficiency under cost-based ratemaking. The PPA is a cost-based rate with two incentive components, and there is nothing inconsistent with the inclusion of incentives in cost-based ratemaking.

---

[10] *Incentive Ratemaking for Interstate Natural Gas Pipelines, Oil Pipelines, and Electric Utilities; Policy Statement on Incentive Regulation*, 61 FERC ¶ 61,168 (1992) (*Incentive Ratemaking Policy Statement*).

[11] *See, e.g., UtiliCorp United*, 95 FERC ¶ 61,054 at 61,130 n.17 (2001) (Commission not precluded from determining what refunds are required under a formula rate in a later proceeding); *Appalachian Power Co.*, 23 FERC ¶ 61,032 at 61,088 (1983) (same); *Kentucky Utilities Company*, 29 FERC ¶ 61,159 (1984).

29. To the extent that the *Incentive Ratemaking Policy Statement* applies to the PPA, the points raised by IEP do not lead us to conclude that the incentive provisions are unjust and unreasonable. For example, IEP's argument against the use of a single source for the indices is not relevant. The Commission does not have a multiple index requirement for incentive-based rates,[12] and IEP did not protest the one that Mountainview used in this proposal. In addition, IEP's argument regarding the use of non-cost-based automatic adjustments for the availability incentives is misplaced. The indices used to escalate the Availability Payments are not "value-based" but inflation-based, and are necessary to hold the value to Edison's customers constant in real dollars. The *Incentive Ratemaking Policy Statement* allows for automatic rate adjustment, and nothing in it precludes the type of indices proposed here.[13] Accordingly, IEP's request for rehearing regarding the incentive provisions is denied.

C. Affiliate Transaction Issues

1. Prospective Application of *Edgar* Standard

30. In the February 25 Order, the Commission accepted the PPA on the basis that it was consistent with our existing policy, but required that in the future all affiliate long-term power purchase agreements, whether at cost or market, will be subject to the conditions set forth in *Edgar*. The Commission explained that, for a variety of reasons, in many regions of the country market prices are below cost-based rates, and expressed the concern that a buyer may potentially favor the rates offered by its affiliate seller over lower rates offered by other nonaffiliated sellers. The Commission was concerned that granting undue preference to affiliates, whether through market-based or cost-based transactions, could cause long-term harm to wholesale competitive markets. Thus, the Commission determined that, in order to protect wholesale power customers and guard against self-dealing in markets where cost-based rates may exceed market rates, *Edgar* will be applied to all future power purchase agreements involving affiliates.

31. The Commission declined to apply the policy announced in the February 25 Order to Edison in order to avoid regulatory impact on transactions already filed for Commission approval. Thus, Edison did not have to meet the requirements of *Edgar*, nor would any other applicants who had filed proposed cost-based rate affiliate transactions under FPA section 205 as of February 25, 2004.

32. IEP, Calpine, and Competitive Suppliers argue on rehearing that the Commission should have applied the requirements of *Edgar* to Edison in the February 25 Order. They contend that the competitive concerns discussed in the February 25 Order are the same concerns recognized by the Commission in *Edgar* and several recent affiliate transaction

---

[12] *See Incentive Ratemaking Policy Statement*, 61 FERC at 61,602-03.

[13] *Id*. at 61,601.

cases,[14] and that in each case, the Commission set for hearing certain issues related to preferential treatment of marketing affiliates. They conclude that the Commission's policy at the time the February 25 Order was issued was that an "*Edgar*-style review of intra-corporate transactions, regardless of whether such transactions purportedly are cost-based, market-based or something in between,"[15] was required. IEP asserts further that Edison knew that *Edgar*-style scrutiny would be required because it included in its application a benchmark analysis intended to satisfy *Edgar* review.

33. IEP and Calpine assert that the Commission failed to explain how the concerns expressed in the earlier cases differed from the concerns identified in the protests in this proceeding, and failed to materially distinguish Edison's proposed transaction from those considered in *Cinergy*, *Ameren*, *Entergy*, and *Southern*. Competitive Suppliers argue that the Commission made a distinction without a difference when it held that cost-based transactions did not require scrutiny under the *Edgar* standard. Calpine and Competitive Suppliers also raise policy implications they contend the Commission did not consider when deciding to exempt Edison from *Edgar* scrutiny, including: (1) the possible harmful impact of the transaction on competition in the California market; (2) an apparent transfer of wealth to Edison shareholders; and (3) the perception by industry experts that the Commission sanctions the re-regulation and re-integration of generation assets into regulated utilities.[16] These parties conclude that the February 25 Order was "a serious blow to a viable competitive wholesale market."[17]

34. We disagree that the Commission ever established a policy requiring cost-based filings under FPA section 205 to meet the *Edgar* standard. The orders that IEP cites do not govern the standard of review for this case. *Cinergy*, *Ameren*, and *OG&E* involved dispositions of jurisdictional facilities; they were filed under section 203 of the FPA,

---

[14] These cases include: *Cinergy Services, Inc., et al.*, 102 FERC ¶ 61,128 (2003), *reh'g denied*, 108 FERC ¶ 61,250 (2004) (*Cinergy*); *Ameren Energy Generating Co., et al.*, 103 FERC 61,128 (2003), Opinion No. 473, 108 FERC ¶ 61,081 (2004) (*Ameren*); *Entergy Services, Inc., et al.*, 103 FERC ¶ 61,256, *reh'g denied*, 105 FERC ¶ 61,208 (2003) (*Entergy*); *Southern Power Company*, 104 FERC ¶ 61,041 (2003); *reh'g pending* (*Southern*); and *Oklahoma Gas and Electric Company, et al.*, 105 FERC ¶ 61,297 (2003), *reh'g pending* (*OG&E*).

[15] IEP rehearing at 10.

[16] Calpine appends to its rehearing several articles purportedly demonstrating these effects. *See* Calpine rehearing, Appendices A, C, and D.

[17] Calpine rehearing at 8.

involving a separate and distinct analysis and standard of review. These orders addressed the effects on competition, rates and regulation that would result from the proposed transfers of jurisdictional assets, but did not involve *Edgar* review. As of the issuance of the February 25 Order, the Commission had not determined to review section 203 applications based on the standards developed in *Edgar*, although that change in policy was recently announced.[18] *Entergy* and *Southern*, which set for hearing PPAs between affiliates, involved market-based rate transactions. It is not the case that we are excusing Edison from *Edgar* review, as parties assert. Rather, it was never a requirement to begin with, and we merely announced a change for prospective implementation in the February 25 Order.

35. Parties are incorrect in arguing that there is no material difference between cost-based and market-based rates in this context. Prior to the policy announced in this case, the Commission conducted only cost-of-service analyses for applications involving cost-based affiliate transactions, and only analyzed market power and barrier to entry factors when considering market-based affiliate transactions. As of the February 24 Order, the Commission will still do a cost-of-service review, but will also look for affiliate abuse and competitive harm by applying the *Edgar* standard of review to cost-based as well as market-based affiliate transactions. Hence, the criteria by which the Commission determines whether these transactions are just and reasonable are distinct. In addition, the Commission has prohibited utilities with market-based rates from making sales to their affiliates absent a separate section 205 filing. The concern has been the potential for cross-subsidization at the expense of the public utility's captive customers. We departed from current policy by calling for *Edgar* review for cost-based affiliate transactions, and, in our discretion, elected not to apply the changed policy here. Had the Commission required review using *Edgar* standards in the February 25 Order, the applicants may have argued with at least some force that we erred by applying a new policy retroactively where the parties had been proceeding in reliance on the established legal regime. The Commission reasonably chose to make the change on a prospective basis effective as of February 25, 2004.

36. Any perception by market participants that the Commission favors re-regulation or re-integration is inaccurate. As discussed in recent orders such as *Entergy* and *Ameren*, we are concerned about recent trends in energy markets, and we now will require additional scrutiny and a greater degree of certainty that affiliate transactions will not cause long-term harm to wholesale competitive markets

.

---

[18] *See Opinion No. 473*, 108 FERC ¶ 61,081 at P 53, 59.

37. While it is true that Edison included in its application a benchmark analysis purporting to satisfy *Edgar* review, as IEP notes, Edison argued in its application that the *Edgar* standard should not apply.[19] The Commission did not make any findings with respect to whether that benchmark analysis would have satisfied *Edgar*, but we note that it did not contain all of the comparable transaction data typically found in an *Edgar* analysis. Edison may well have conducted the acquisition differently if it had known at the beginning that the Commission would require it to satisfy *Edgar* and be able to provide all of the requisite data. Moreover, we considered the entirety of Edison's application and imposed conditions to prevent the type of affiliate abuse that the *Edgar* standard was designed to address.[20]

38. We also disagree that an evidentiary hearing was warranted in this case. The courts have repeatedly recognized that the Commission has broad discretion in managing its proceedings.[21] The Commission may properly deny an evidentiary hearing if the issues, even disputed issues, may be adequately resolved on the written record, at least where there are no issues of motive, intent, or credibility.[22] Based on the pleadings submitted in this proceeding, we concluded that there were no issues of material fact that were best resolved through a trial-type evidentiary hearing.

2. <u>Monopsony</u>

39. In response to assertions that Edison would harm wholesale competition by exercising its monopsony power as the sole buyer in its territory, the Commission found in the February 25 Order that intervenors had not demonstrated that Edison exercised

---

[19] *See* Edison transmittal letter at 53 – 61.

[20] *See* February 25 Order at P 63 (explaining that the marginal cost bidding condition for resales by Edison of the output from Mountainview would address concerns related to affiliate abuse).

[21] *See Vermont Yankee Nuclear Power Corp. v. Natural Resources Defense Council, Inc*., 435 U.S. 519, 524-25 (1978) (agencies have broad discretion over the formulation of their procedures); *Florida Municipal Power Agency v. FERC*, 315 F.3d 362, 366 (D.C. Cir. 2003); *Telecom Resellers Assoc. v FCC*, 141 F.3d 1193, 1196 (D.C. Cir. 1998); *Alabama Power Company v. FERC*, 993 F.2d 1557, 1565 (D.C. Cir. 1993); *Michigan Public Power Agency, et al. v FERC*, 963 F.2d 1574, 1575, 1578-79 (D.C. Cir. 1992) (Commission has discretion to mold its procedures to the exigencies of the particular case); *City of Lafayette, Louisiana v. SEC*, 454 F.2d 941, 953-5 (D.C. Cir. 1971) (same).

[22] See *Texaco, Inc. v. FERC*, 148 F.3d 1091, 1100 (D.C. Cir. 1998).

such power here. The Commission explained that IEP had not shown why the relevant market in this case is so constrained as to allow the exercise of monopsony power and why a seller in Edison's territory does not have the ability to sell to utilities in other parts of California or the West.

40. IEP argues on rehearing that intervenors had shown that Edison had significant monopsony power and that the Commission erred by not addressing the exercise of Edison's monopsony power and the increase in Edison's monopsony power resulting from the PPA. IEP asserts that Edison is a monopsonist in its territory and that the Commission was wrong in its February 25 Order when it suggested that the relevant geographic market was all of California and the West. IEP states that, at a minimum, the issue of the relevant geographic market should have been set for hearing.

41. We will deny IEP's request for rehearing on the question of Edison's monopsony power and the relevant geographic market. IEP argues that sellers in the area have no other alternative but to sell to Edison and that the Edison control area should be considered the relevant geographic market for analyzing the effect of the PPA. IEP cites the Commission's finding in another recent order, where the relevant geographic market was the utility's service territory and states that the same should hold here.[23] IEP fails to note that, unlike Oklahoma Gas and Electric, Edison does not control its transmission system, and cannot, therefore, use its transmission to exclude competition. We considered IEP's argument and found that Edison did not have the ability to prevent sellers from selling to other buyers outside of Edison's service territory. We noted in the February 25 Order that Edison's transmission system is operated by an independent system operator (ISO), which gives sellers more opportunities to sell outside of Edison's service territory.[24] Likewise, in *AEP*,[25] the Commission found that, absent a showing of persistent transmission constraints, the entire ISO or regional transmission organization should be considered the default relevant geographic market for market power analyses.

42. IEP also argues that Edison can exercise vertical market power through strategic dispatch of Mountainview and requests that we require Edison to submit a study examining the impact of its dispatch decisions on transmission constraints faced by competing sellers.[26] However, given the fact that Edison's transmission system is

[23] IEP at 23, *citing* Oklahoma Gas and Electric Company and NRG McClain LLC, 105 FERC ¶ 61,297 (2004).

[24] February 25 Order at P 41.

[25] *See AEP Power Marketing, Inc., et al.*, 108 FERC ¶ 61,026 at P 31-36 (2004) (*AEP*).

[26] IEP at 36.

controlled by the California Independent System Operator (CAISO), absent a showing of actual instances of Edison creating transmission constraints on the system through strategic dispatch of Mountainview, we would not expect Edison to possess such ability. This issue has arisen in the context of a vertically integrated utility with both transmission and generation assets acquiring additional generation and/or transmission assets.[27] However, in those cases, we have held that turning over operational control to an independent transmission operator sufficiently mitigates any such ability. In addition, if Edison is, indeed, able to create persistent transmission constraints through its dispatch of Mountainview facility, then the relevant geographic market should be adjusted in Edison's market-based rates application or three year update, and the Commission would review that under Edison's market-based rate authority. In any event, we will not require Edison to file a study in this proceeding, as IEP requests.

3. **Resales Into Spot Market**

43. One of the conditions placed on Edison in the February 25 Order was to restrict Edison's resales of the output from Mountainview to spot market sales bid at the marginal cost of each unit. The Commission took this measure in response to concerns that Edison could market its purchased power from Mountainview and receive market-based compensation, thereby changing market outcomes by bidding energy or capacity from Mountainview into the CAISO's market below its costs. The Commission noted that because Edison is assured full cost recovery of its cost from Mountainview, it could benefit from such a bidding strategy if it depresses a clearing price and is a net buyer. Thus, requiring any such resales to be bid no lower than marginal would prevent Edison from depressing the clearing price.

44. IEP argues that it was arbitrary and capricious for the Commission to allow resales of the Mountainview output into the spot market because: (1) allowing such resales by Edison is inconsistent with Edison's commitment that the Mountainview output will be used only for resale to its customers; (2) the Commission-imposed restriction on Edison's sales of the Mountainview output into the spot market is unenforceable because Edison can evade the restriction by increasing sales from the Mountainview plant to allow other Edison units to sell into the spot market; and (3) the marginal cost bidding requirement for Edison's sales of the Mountainview output into the spot market does not address the harm to competition because Edison can still recover its fixed costs through the PPA even if the spot price is equal to its marginal costs whereas other sellers do not recover fixed costs when they sell at marginal cost, which they argue gives Edison the "safety net"

---

[27] *See, e.g., American Electric Power Company and Central and South West Corporation*, Opinion No. 442, 90 FERC ¶ 61,242, *order on reh'g*, Opinion No. 442-A, 91 FERC ¶ 61,129 (2000).

advantage that troubled the Commission in *Cinergy* and *Ameren*.[28] IEP argues that the Commission should impose a refund condition on all Edison spot sales and set for hearing the issue of how to minimize the subsidization of Edison's market sales described above.

45. We will deny IEP's request for a refund condition and hearing. Our February 25 Order noted that the PPA limited Mountainview's sales to cost-based sales to Edison and sales into the ISO market in response to CAISO dispatch orders. We noted that as a net buyer, Edison has incentive to bid low in order to lower the spot market price. By establishing a marginal cost bidding requirement, we have eliminated Edison's ability to artificially lower the spot price with its control of the Mountainview output.

46. Regarding IEP's argument that Edison has a competitive advantage because it can still recover its fixed costs through the PPA even if the spot price is equal to its marginal costs whereas other sellers do not recover fixed costs when they sell at marginal cost, we note that only the marginal seller in a given hour does not recover any fixed costs (assuming it bids its marginal cost). All other sellers with marginal costs lower than the clearing price do recover some fixed costs. In addition, we note that the CAISO is considering implementing capacity markets to provide a mechanism for additional cost recovery for generators. Finally, IEP's reference to the safety net issue in *Cinergy* and *Ameren* is misplaced. In *Cinergy* we noted that "[t]he ability of a franchised utility <u>to assume its affiliated merchant's generation when market demand declines</u> gives the affiliated merchant a 'safety net' that merchant generators not affiliated with a franchised utility lack"[29] and we expressed concern that "the existence of a safety net may affect the incentive of new merchant generators to invest in new facilities," erecting a barrier to entry that harms the competitive process and raises prices to customers in the long run "because affiliated merchant generation with a safety net option will not be subject to the price discipline of a competitive market."[30] The "safety net" did not pertain to an affiliated generator's ability to always profitably bid at marginal cost; rather, it related to an affiliated merchant generator having the advantage of being acquired and rolled into its affiliate's rate base during times of soft demand conditions relative to available supply.

47. Regarding IEP's second argument, we recognize that Edison has a portfolio of assets from which it buys and sells power. However, buying power from Mountainview in order to free up other generation resources to sell into the ISO, as described by IEP, would only be profit-maximizing when the Mountainview output is lower-cost than

---

[28] IEP at 28-30, *citing Cinergy* and *Ameren*.

[29] *Cinergy*, 102 FERC ¶ 61,128 at P 23 (emphasis added).

[30] *Id*.

Edison's other resources, in which case economic efficiency would be increased, not decreased as argued by IEP. In such a case Edison would indeed have capacity "freed-up" to sell into the market, but that incremental capacity would only be called to the extent its bid were lower than other bids – thus crowding out higher-cost power from other suppliers. As we noted in the February 25 Order, Edison would have had the incentive to try to lower the spot when participating as a net buyer prior to entering into the PPA; the PPA actually reduces this incentive by decreasing Edison's net short position. Our concern was that the PPA could increase Edison's ability to affect the spot market price. We addressed that concern by imposing the marginal cost bidding rule, which eliminates Edison's ability to affect the spot market price through its bidding the Mountainview output into the spot market. Whatever ability Edison had to lower the spot market price remains the same – every MW that is freed-up to sell in to the spot market is the result of a MW of energy from Mountainview being used to reduce Edison's net short position.

48. IEP also argues that the full output is not needed by Edison until 2010 and that, at times, Edison will be a net seller into the CAISO market. IEP is arguing that Edison has, at various times, the ability and the incentive to either raise or lower the price in the ISO spot market, depending on whether it is a net buyer or net seller. However, the conditions of the February 25 Order remove the ability of Edison to lower the spot market price when it is a net buyer, and the conditions of Edison's market-based rate authority (along with the ISO's market power monitoring and mitigation) address the possibility that Edison could raise the market-clearing price when it is a net seller. That is, Edison has been found to lack generation dominance and is subject to the market behavior rules in its market-based rate tariff.[31] Moreover, when Mountainview becomes operational, Edison will have to show the Commission that it still warrants market-based rate authority.[32] Thus, any concerns regarding Edison's exercise of either buyer market power or seller market power are addressed by the conditions of the February 25 Order and Edison's market-based rate authority.

[31] *See Southern California Edison Company*, unpublished letters orders in Docket Nos. ER02-2263-000 (Aug. 29, 2002) and ER02-2263-002 (Mar. 29, 2004).

[32] We note that, under the current standard, Edison would be required to file an updated market power study in its triennial review of its market-based rate authority. In Docket No. RM04-14-000, the Commission recently issued a Notice of Proposed Rulemaking regarding the reporting requirements for changes in status for public utilities with market-based rate authority, proposing that changes of status be reported to the Commission within 30 days. *See Reporting Requirement for Changes in Status For Public Utilities With Market-Based Rate Authority*, 109 FERC ¶ 61,021 (2004).

4. Clarification of *Edgar* Standard

49. Competitive Suppliers urge the Commission to clarify in this order several aspects of a making a successful *Edgar* showing. Specifically, they request that the Commission provide key issues, definitions and information requirements that will indicate a utility's supply contracting or asset transfer with an affiliate is the result of a fair and transparent evaluation process. They recommend milestones and characteristics described in a guidebook recently published by EPSA and particularly wish to see a requirement for the use of an independent third-party to oversee solicitation processes. Should the Commission not make such clarifications, Competitive Suppliers request rehearing.

50. We will refrain from clarifying requirements for making an *Edgar* showing in this proceeding. The Commission has instituted an inquiry in Docket No. PL04-6-000 to explore solicitation processes for power procurement, including solicitations whereby public utilities sell to their affiliates. Any further clarification or requirements for affiliate transactions will be addressed in that docket.[33]

D. PURPA Issues

51. In the February 25 Order, the Commission rejected arguments that we should condition our approval of the PPA in a way that requires continued compliance with PURPA by Edison. The Commission responded that we are not required to make any findings in this proceeding about Edison's PURPA obligations and explained that the applicable standard for approval of the PPA is whether the rate is just and reasonable.

52. On rehearing, CAC asserts that the Commission erred by approving the PPA without appropriate conditions ensuring compliance with PURPA. CAC restates its earlier contention that the Commission may not approve the PPA if that approval "would result in a violation of or disregard for the provisions of PURPA."[34] CAC notes that the February 25 Order conditioned approval on Edison and Mountainview agreeing to certain specific conditions and argues that the same should apply to Edison's commitments regarding its PURPA obligations.

53. CAC raises no arguments on rehearing that we did not previously consider, and we will deny its request for rehearing. CAC is confusing the findings that must be made concerning filings made under FPA section 205 and separate proceedings implicating PURPA. The Commission did not find, and was not required to find, that the proposed

---

[33] *See also Allegheny Energy Supply Company, LLC*, 108 FERC ¶ 61,082 (2004) (providing further guidance regarding Commission standards by which we review market-based rate affiliate sales resulting from RFP processes).

[34] CAC request for rehearing at 9.

transaction was in the public interest; rather, the standard of review was whether the proposed transaction results in rates that are just and reasonable and not unduly preferential or discriminatory. All of the conditions imposed in the February 25 Order were meant to ensure that the proposed rate will be just and reasonable. The issue that CAC raises, *i.e.*, "whether Edison's acquisition of Mountainview will in any way obstruct its continuing compliance obligations under PURPA,"[35] is beyond the scope of this proceeding, and CAC has other avenues to object should future actions of Edison appear to compromise its obligations under PURPA.

The Commission orders:

(A) The requests for rehearing of the February 25 Order are hereby denied, except with respect to Prior Claims, as discussed in the body of this order.

(B) Edison, on behalf of Mountainview, is hereby directed to submit a compliance filing within 30 days of the date of this order revising the PPA, as discussed in the body of this order.

(C) Calpine's motion to lodge is hereby denied.

By the Commission. Commissioner Kelly not participating.

(S E A L)

Linda Mitry,
Acting Secretary.

[35] *Id.* at 4 and 8.